Merchandising Trends
Drug store housewares sales climb—p. 35

'86 Annual Report
Exploring wholesaler trends—p. 13

C.E. Lesson
New antiarrhythmics—p. 79

DRUG STORE NEWS

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Pay 'n Save's Nathanson to walk fiscal tightrope

Can 'strong leader' halt chain's losing streak?

By Lou Karney

SEATTLE — When Gerald Nathanson replaced Allen Culver as vice-chairman and ceo of Pay 'n Save drug stores, it signaled the chain's continued commitment to the Zimmerman merchandising strategy.

Nathanson's 22-year career has "general merchandise" stamped in boldface—and that's the core of the Pay 'n Save marketing plan.

The question buzzing the trade is: What changes will Nathanson make in the Zimmerman concept? "It's too early to talk about," Nathanson told *Drug Store News*. "I've only been here a week."

The Zimmerman strategy has already undergone several alterations. Originally, the prototype for retrofitted Pay 'n Save drug stores consisted of up to 50 6x3 promo tables. They were located front-and-center, at the start of the horseshoe-shaped race track layout.

Strategy adjusted

Merchandise on the tables are closeouts, special buys, imports and overruns, which are being sold at 30%-70% below what other retailers charge and still manage to achieve a gross profit of 50%.

Several months ago, the aisles were widened from 11 to 14 ft., and the number of tables reduced to 25. But the crux of the move is that

Gerald Nathanson

the tables are now placed alongside the race track, thus freeing space for 192 ft. of gondola, which was used to expand seasonal goods and greeting cards.

In October, William Zimmerman, Pay 'n Save chair-

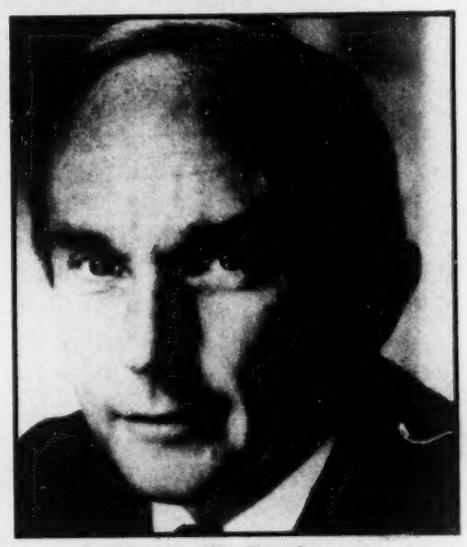
See **Pay 'n Save,** *page 87*

Hook-SupeRx LBO takes shape under new ceo

By Dave Vaczek

CINCINNATI — Kroger said it will sell 710 SupeRx and Hook drug stores to a private group led by Philip E. Beekman, a former president of Joseph E. Seagram & Sons, who will head the new company as president and ceo. The new firm is tentatively called Hook SupeRx Inc.

The leveraged buyout, which sources said was being developed the past month, doesn't include the two top managers of the drug division: president Gerald Wolken and executive vp-operations J. Douglas Reeves. They won't be part of the manager-investor group who will buy the stores with Beekman and other unnamed investors. Kroger will hold up to a 40% stake in



Philip E. Beekman

the new company, sources said.

The new company will be made up of drug stores clustered primarily in Ohio, Indiana, Illinois, Kentucky, Tennessee, West Virginia and Virginia.

Sale of remainder

The remaining 180 units in the 890-store division, as reported will be put on the market: 39 Phoenix units, 106 in Florida and 35 in Alabama and Georgia. Lehman Brothers will arrange those sales.

See related stories, p. 3

Analysts estimate Kroger will collect $300 million to $500 million on the sale of all its drug stores, which it announced this year as part of a strategy to achieve long-term profitability with other retail formats.

"The No. 1 priority right now is to get this transaction

See **Hook,** *page 88*

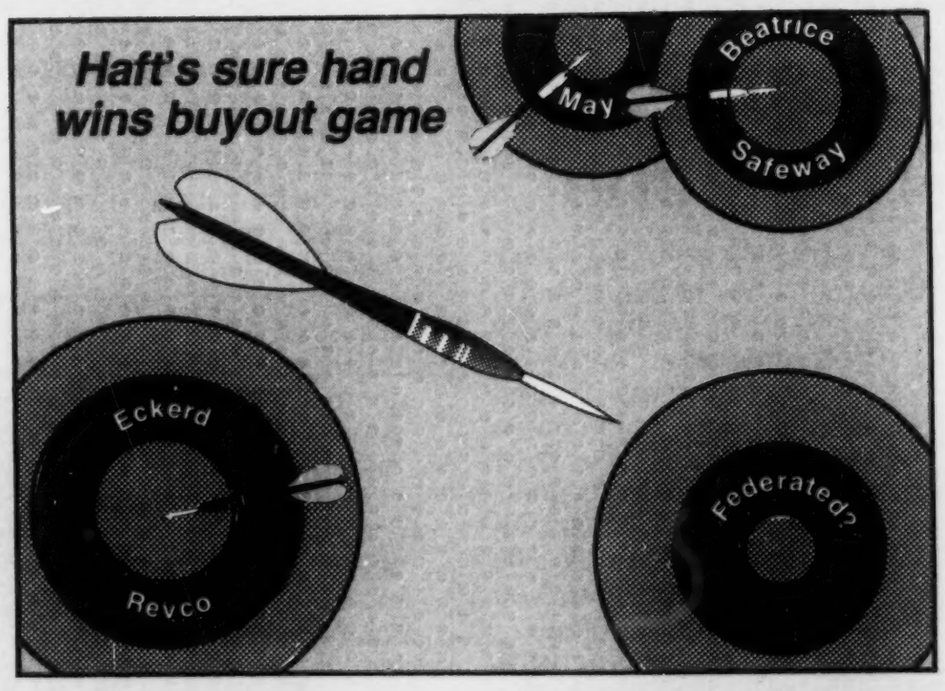
Dart Group flexes acquisition muscles

Sells its option back to Safeway for $59M

LANDOVER, Md. — The Dart Group is tramping down the acquisition trail with renewed vigor, after selling back to Safeway for $59 million an option to buy a part of the reorganized Safeway stores. Dart also said it isn't interested in buying Safeway divisions it was assessing.

"It looks like they're swinging for the fences. They want to have the image of being in the big leagues in mergers and acquisitions," said Jerome Kaplan, a Value Line analyst.

Dart Group agreed to sell its option for 20% of the new Safeway company being formed by Kohlberg Kravis Roberts investment firm, and also passed up the chance to buy certain divisions. The proceeds and savings will fortify a war chest targeted for new buyout prospects.



The $59 million proceeds add to the $80 million Dart reportedly cleared when it sold its 5.9% Safeway stake to KK&R.

By selling its Safeway interest, Dart owners Herbert and

See **Safeway,** *page 88*

Wall St. speculation focuses on Federated

NEW YORK — Investors' speculation that the Dart Group has returned to the buyout arena prompted a $3.75 per share jump in Federated Department Stores stock, analysts said.

Wall Street sources said conjecture that Cincinnati-based Federated might be Dart's next victim accounted for a price rise to $94 on Oct. 23 (at presstime).

Department stores are attractive buyout candidates for

See **Federated,** *page 88*

2 groups eye Gray Drug Fair buy

CLEVELAND — At least two groups—one headed by Al Towle and another made up of Gray Drug Fair management—have expressed interest in acquiring the 420-store drug chain from Sherwin-Williams through a leveraged buyout, according to industry sources.

Sherwin-Williams, which has reportedly received no acceptable outside offers, has conceded that it would now consider an LBO by an inside management group. The proposed sale is being handled by Goldman Sachs.

The diversified paint manufacturer and retailer announced in July that it had placed its drug chain on the auction block in order to "concentrate on our coatings and coatings-related business."

Sherwin-Williams, which acquired the chain in 1981, has experienced five years of up and down results. The most recent performance, however, points to an upward trend.

Al Towle, 48, is the former president and general manager of Gray Drug Fair who was dismissed three years ago, reportedly because his progress in turning around the troubled drug chain was not fast enough to suit Sherwin-Williams.

His departure began a revolving door management cycle in the top executive suite. Other presidents who have since come and gone include Al Culver and Jim Mastrian. Carl Bellini, the current president and reported leader of the LBO group, has also occupied the president's chair during several interim periods.

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Revco sheds subsidiary to help fund LBO

But pact with PFI remains

TWINSBURG, Ohio — Revco will raise about $16 million to help fund its pending leveraged buyout by selling its subsidiary that makes generic drugs, vitamins and packaging.

The chain has contracted to sell Private Formulations to PharmaControl Inc., a publicly owned drug manufacturer headquartered in Englewood Cliffs, N.J., a spokesman for PharmaControl told *Drug Store News*.

PharmaControl managers have already taken an active operating role in the company, although the sale is contingent upon financing. The company expects to pay a $1 million premium above a $15 million auditors' valuation of assets, which include a 215,000-sq.-ft. warehouse and manufacturing equipment, the spokesman said.

'Take-or-pay' pact

The pact includes a five-year "take-or-pay" requirement, under which Revco must continue to buy products from Private Formulations at near its current purchase level, currently about 50% of the PFI's $24 million in annual sales. PFI manufactures and distributes about 1,200 products, including pain relievers, antacid and allergy remedies, cough suppressants and laxatives.

Revco management is expected to eye the sale of its nonretailing subsidiaries as a way to raise cash to help service LBO debt. And by selling nonretail businesses, Revco will focus on the core drug store operations—an effort that began earlier this year when Revco spun off its General Computer Corp. into a new public company, but retained a minority interest.

Vertical integration

Revco subsidiaries have supported a vertical integration strategy. They make store fixtures, generic drugs, construction equipment and nursing home prescription services. They have contributed about 5% of total revenues. Revco has owned PFI since the early 1970's.

The buy will boost PharmaControl's annual revenues from $3 million to over $25 million. Besides buying the business of Private Formulations, PharmaControl will use the manufacturing and distribution capacity to develop new drug products. The Edison plant was reportedly underutilized, and its facilities can support about $70 million in sales.

"It's a good buy. But it's not a steal. There's a lot of surplus manufacturing capacity in the industry right now," said a source close to the sale.

In an unrelated matter, Revco said it has settled more than 75% of the cases involving infants treated with E-Ferol, the vitamin product made by its Carter-Glogau Laboratories subsidiary. It said it expects a "substantial portion" of the costs of the settlements will be recoverable from state insurance and from the chain's claim against two involved insurance carriers, who have been placed in bankruptcy liquidation.

Revco subsidiaries

Carter-Glogau Laboratories Inc.	Manufactures sterile injectable medicaments
Crown Store Equipment	Manufactures and installs metal and wood store fixtures
Insta-Care Pharmacy Services	Provides pharmacy services to nursing homes
Revco Optical Centers	Eyeglass and contact lens stores
Stanton Corp.	Leases and sells polygraph and written honesty tests
Waco Equipment Corp.	Leases and sells construction equipment, scaffolding and trailers
Barre National	Manufactures liquid generic products
Odd Lot Trading Co.	Sells closeout retail merchandise
Private Formulations	Makes generic drugs, vitamins and packaging

Revco's subsidiaries are prospects to be sold to raise cash to support management's leveraged buyout, Wall Street and industry sources said.

Source: *Drug Store News* research

NEWS IN BRIEF

Vons/Allied merger kaput

EL MONTE, Calif. — The proposed merger of Vons Grocery and Allied Supermarkets of Detroit—valued at $660 million—has been called off. The reason, according to David Page, chairman and ceo of Allied, was difficulty in resolving a number of unspecified issues.

As a result of the breakoff, Allied was the loser on Rx-drug operations. Vons, operating 40 pharmacies in its combos, is a major marketing force in southern California, while Allied's Rx performance in the Midwest is weak. Allied closed five of its six freestanding Family Drug Stores (10,000-20,000 sq. ft.) a year ago because they were not profitable.

Allied had hoped that "shared ideas"—that is, borrowing from Vons' extensive know how—would beef up Allied's performance on the drug side.

Perry honors pharmacists

PONTIAC, Mich. — Perry Drug has named six pharmacists to receive its first Pharmacist of the Year award, recognizing their professional work and involvement with patients and the community.

Each winner received an engraved plaque and $500 during presentations at Perry's Christmas vendors' show in October.

The chain took out a full-page ad in the Detroit *Free Press* congratulating the winners, whose awards coincided with Michigan Pharmacy Week.

The recipients are: Phil Connor, 38, Pontiac, Mich.; George Didur, 27, Pontiac; Joann Frederick, 35, Rochester, Mich.; Bob Jasinski, 48, Rochester Hills, Mich.; Thaddeus Setla, 37, Ortonville, Mich; and Myron Sonkin, 35, Lisle, Ill.

INDEX

Beauty Beat 9	Merchandising Trends 35
Classified 87	People in the News 30
Editorial 4	Product Update .. 32
Financial 6	Wholesaler Report 13
Focus on People 33	
Inside Pharmacy . 37	

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Walgreens expands DC in Arizona

FLAGSTAFF, Ariz. — Walgreens has begun to build a 125,000-sq.-ft. addition to its distribution center here—its western-most in the United States—to support planned growth of 30 units in the West through 1987, the chain said.

The $10 million expansion will enlarge the DC to 325,000 sq. ft. and will be in operation by June, the company said.

Walgreens said in August it plans to add 30 stores in the West, particularly in Phoenix and San Francisco. The DC now supplies merchandise to about 200 stores in Arizona, California, Colorado, New Mexico and parts of Texas. It supplies 80% of store merchandise, with a one-day delivery reach to all markets.

Parts of the DC upgrade are changes in the conveyor system and installation of "walk and pick" product handling systems that allow workers to fill portions of seven orders at once.

Merchandise in the new area will be stacked on 28-ft.-high racks, substantially increasing storage capacity.

Northwestern continues repositioning efforts

AUBURN, Wash. — Northwestern Drug is well into a multipronged program to reposition itself after 2½ years of laboring to keep market share under Pay 'n Save ownership.

Efforts to revitalize the regional wholesaler include acquisitions, formation of a new buying group, faster prescription drug delivery services and a management restructure.

Since Seattle Standard retained ownership control, Northwestern has been moving to get past such problems as: some pharmaceutical manufacturers having refused to ship to Northwestern because it was retailer-owned (since settled by lawsuit), and some retailers such as Bartell Drug who viewed Northwestern as a profit feeder for Pay 'n Save and didn't want to support that business.

Acquired VSC

The first acquisition it made earlier this year was VSC Corp., a specialty distributor of paper products and supplies to hospitals, nursing homes and DME retailers.

"VSC provides us with a new level of diversification," said Ed Croke, Northwestern's senior vp. "VSC is a separate entity with its own customer base. It also has its own discrete marketing staff, reporting to Paul Stanfill, former president of VSC."

In addition, Northwestern bought Velocity Hospital Group Oct. 1 to "give us more direct control of the hospital business," Croke said. Formerly, Velocity was a separate company with a long-term contract with Northwestern to supply Northwestern's more than 100 hospital accounts—mainly in the Pacific Northwest.

On the buying front, Northwestern formed VeloGroup, a buying group for generics, last April. "The group has better prices than Northwestern," said Croke, "in that it has achieved cost savings in excess of 20% for our more than 400 retail partners [Northwestern's designation for members]. We are awarding bids on an item-by-item basis, rather than across the breadth of the line."

Northwestern has also sped up Rx-drug delivery service. It used to take 24-30 hours to deliver to distant points such as eastern Washington and most of Oregon. Now it's 16-18 hours.

Bloom becomes chairman

The restructuring places Steve Bloom, who has purchased a substantial ownership interest in Northwestern, as chairman. Parent Seattle Standard retains ownership control. Croke refused to give the purchase price or the percentage investment. Nor would Croke indicate whether the money will be channeled into Northwestern's operation.

Bloom, who has a background in distribution of candy, tobacco and H&BA, was former vice-chairman of Core-Mark International, a U.S. and Canadian distributor with sales of $2.3 billion annually. Bloom's strengths are in finance, management and sales. He also has a keen insight into people and a high energy level, a Northwestern executive said.

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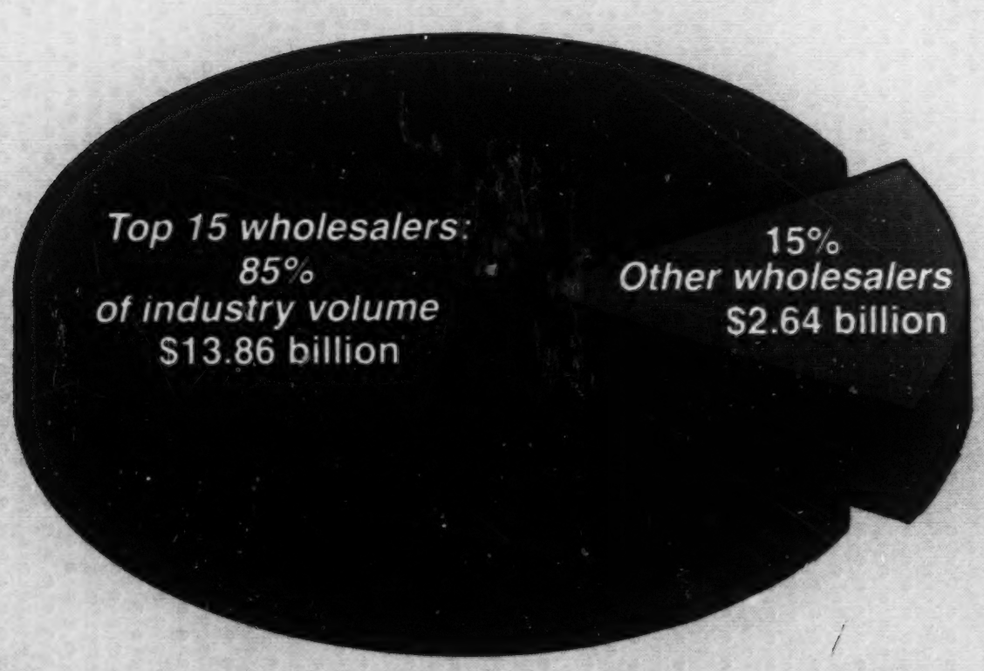
The 1986 Annual Report of the Wholesale Drug Industry



Source: *Drug Store News* analysis

Wholesale giants shaping industry

By Liz Parks

The year 1985 was disappointing for drug wholesalers, and 1986 is not shaping up much better.

But as this industry continues evolving into an oligarchy, the last half of this decade could usher in an era of industry stability and profitability.

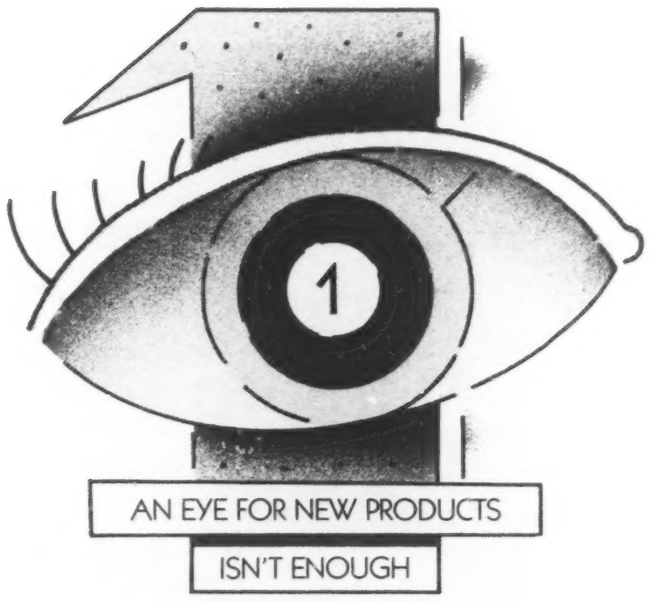
Net profit margins, which were almost at the 2% level in 1982, dropped to 1.47% in 1985, down from 1.78% in 1984. Gross profit margins, which were at 11% in 1982, dropped to 8.86% in 1985, down from 9.74% in 1984.

Wall Street analysts and executives in the major drug wholesaling companies don't see this trend abating, possibly even in 1987, but some see indications that things are getting better. A few speculate that in two or three years, there will be just four or five companies controlling 90% of total sales. At that point, "the fierce competitive phase of the industry will be over," and profits will stabilize.

Although these sources see the profit erosion continuing for "a few more years," margins will eventually rebound as the five or six major companies in the industry complete their acquisition campaigns, digest their mergers and consolidate their strength.

As the Big Five achieve their individual optimum market share gains, these sources say, they will begin to operate in what FoxMeyer chairman Bill Tauscher calls "a more realistic manner." That means they will eliminate price and bidding wars, concentrate on building margins and continue to use their growing economies of scale to find new operating efficiencies that will trickle down to the bottom line.

Continued on page 14



'86 ANNUAL WHOLESALER REPORT

Dwindling inflation blamed

Changes in customer mix

- In 1985, wholesale sales to independent drug stores continued their long-term decline.
- At the same time, drug wholesaler sales to less traditional trade areas like chain drug stores and hospitals increased to an all-time high.
- In 1978, drug wholesalers did 62.4% of their overall business with independents and just 20.6% with chains and 10.9% with hospitals.
- In 1985, however, the NWDA operating survey revealed that just 50% of a drug wholesaler's overall sales were with independent drug store retailers, down 3.44 percentage points from 1984.
- At the same time, drug wholesalers were now doing 23.16% of their total sales with chain drug stores direct, compared with just 19.66% in 1984. In addition, drug wholesalers in 1985 were doing 19.47% of their overall business with hospitals, compared with 18.61% in 1984.

Continued from page 13

In analyzing what the 1985 profitability slump means for the industry in terms of its long-term stability, most sources cite a variety of factors that accounted for the decline in 1985.

These include the waning of inflation; the problems for the major companies of "digesting" the 30 or so acquisitions that occurred during 1984 and 1985; the expansion of retail buying groups, which forced many wholesalers into more competitive pricing structures; the withdrawal from secondary suppliers as alternative sources for pharmaceutical supplies; the cutthroat competition for an increased share of the low-margin, but high-tonnage hospital business; and the manufacturer practice of offering differential prices, which wholesalers say still exists and still creates an "unfair competitive environment."

Although no wholesaler interviewed by *Drug Store News* ventured to say all these elements would disappear over the next year or so, most did say there are indications that relief is in the wind.

'Some manufacturers have implemented policies that would preclude favorable pricing. I hope that this is a trend.'
—Bill Bindley
president,
Bindley Western

Positive factors

Many executives at the bigger companies like Alco, Amfac, Bergen Brunswig, Bindley Western, FoxMeyer, Harris and McKesson point out that they are continuing to centralize and consolidate their operations so that more functions can be performed under one roof and duplications can be eliminated.

Even though most executives say it is getting harder to initiate savings through cost reductions, most add that they can continue to count on technology to improve the bottom line for at least "a little bit longer."

Seth Harris at Harris Wholesalers and Mel Whitmire at Amfac said they are investing in systems that will reduce costs and improve efficiencies.

Amfac has just finished installing a new computer system in all its branches to handle electronic transmissions of data, while Harris over the coming year will be installing a centralized data processing system that will let management run its nine distribution centers all on the same computerized accounting system.

Both companies anticipate enormous productivity gains.

At the same time that wholesalers continue to devise

BULL SHAVERS ARE A DYING BREED.

Consider this ad an obituary.

It's a farewell to Bull shavers —all those men who were convinced they had to pay an arm and a hoof to get a close comfortable shave.

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So doesn't it make sense to take the shelf space from Bull shavers and make room for Bic Shavers instead. Because while Bull shaving is dying, Bic shaving is booming.